J.D. McGREGOR
VICE PRESIDENT, SALES

POGO PRODUCING COMPANY

May 28, 1997

Minerals Management Service
Royalty Management Program
Rules & Procedures Staff
P O BOX 25165, MS 3101
Denver, Colorado 80225-0165

Dear Sir or Madam:

In response to the Department of the Interior, Minerals Management Service (MMS) request for comments regarding the proposed rulemaking establishing oil value for royalty due on federal leases and on the sale of royalty oil, Pogo Producing Company (Pogo) hereby offers the following comments.

Pogo is an independent, publicly traded oil and gas company engaged in exploration, development and production on its properties and the sale of hydrocarbons from such properties which are located, among other places, offshore in the Gulf of Mexico and onshore in the United States. Pogo has a direct and significant interest in this proposed rulemaking and herein conveys Pogo's support for MMS efforts to ensure fair market value for its royalty production. As an independent producer with only arms length transactions for sales of its own production, Pogo endorses MMS efforts to preserve the gross proceeds method of royalty valuation for arms length bargaining. Pogo has absolutely no intention to ever sell production at any price less than the highest price we can negotiate. While it remains the prerogative of MMS to suggest changes in royalty valuation as deemed necessary to secure your interest, equity requires an evenhanded approach to such valuations. In the case of arms length negotiations, equity has only two alternatives - the best price the producer can negotiate, or if dissatisfied with that price, royalty-in-kind. The fact that Pogo routinely receives among the highest prices being paid for crude oil production in their area of production speaks loudly for the gross proceeds method. Indexing and its attendant calculations layers another level of administrative burden on the producer who otherwise would correctly account for oil sales under gross proceeds.

Notwithstanding Pogo's support for the gross proceeds method, Pogo impels MMS reconsideration of the provisions which would require arms length sales to be valued under the proposed index pricing provisions if the producer had purchased any crude oil from an unaffiliated third party in the United States during the two years preceding the production month. Pogo appreciates MMS concern for potential royalty undervaluation; however, presently existing regulations address remedies for such malfeasance. The major area of concern with the two year purchasing rule, insofar as Pogo is concerned, is that often a producer may find certain production is captive to a nonjurisdictional pipeline. In order to make that production available to the best market, the producer will have to transport its production via this non jurisdictional pipeline. The pipeline, however, will only transport barrels it has title to in order to retain its nonjurisdictional status. Therefore, a buy/sell transaction is entered into whereby the pipeline buys the production at the inlet to the pipeline and sells equivalent volumes back to the producer at the terminus of the pipeline at the first sales price plus transportation costs. The producer then resells its production to the purchaser of choice and to the extent royalties are due pays such royalties on the higher of the two sales prices - not the lower. These arrangements capture the entire consideration of the deal and there is absolutely no future consideration or corresponding lateral consideration attached. Pogo believes the two year purchase rule serves to disadvantage the producer - and perhaps MMS - when the producer would otherwise value production under the gross proceeds method.

In the event MMS believes it is receiving less than fair market value for its royalty interest, Pogo believes MMS has the best possible remedy available by exercising its option to take its production in kind. Despite the wholesome intentions of increased compliance, the regulatory highway is less a superhighway than a rural tollroad which we are required to travel and that is filled with the potholes of unintended consequences. Clearly, when less regulation will work - less regulation is called for. In the case of royalty undervaluation, real or perceived, royalty-in-kind offers the least burdened solution for both MMS and the producer.

As a final comment, Pogo registers its vigorous dissent against the MMS position that a producer has a duty, not to just market MMS oil, but to place oil in marketable condition at no cost to the Federal Government. By any measure, the Federal Government should bear the same proportional costs the producer bears in order to make a sale of oil. Pogo remains unconvinced that anything in law or equity requires a producer to absorb any cost which should otherwise attach to the royalty owner.

Pogo appreciates the opportunity to express its views on this matter.

Very truly yours,

J. D. M.